Comhairle Chomhairleach Bhuiséadach na hÉireann
Irish Fiscal Advisory Council

FISCAL ASSESSMENT REPORT

NOVEMBER 2013

Good progress continues to be made in bringing sustainability to the public finances and in restoring the borrowing capacity of the State. Recent signs of growth momentum should continue into 2014. However, ongoing balance-sheet repair and a weak Euro Area growth environment are important downside risks.

The Chair of the Irish Fiscal Advisory Council, Professor John McHale, cautioned that:

"While there is a difficult trade-off between supporting domestic demand and meeting fiscal targets, the decision to do less than the originally planned adjustment in Budget 2014 increases the risk that the key 2.9 per cent deficit ceiling in 2015 will be breached."

Under its revised mandate, the Council endorsed the macroeconomic projections underlying *Budget 2014*. A detailed explanation of the Council's approach to the endorsement exercise is provided in the report.

MEDIA BRIEFING

Members of the media are invited to attend a briefing on **Thursday 21st November at 10.30 a.m.** at the Irish Fiscal Advisory Council, Whitaker Square (ESRI building), Sir John Rogerson's Quay, Dublin 2. The briefing will take place in Conference Room 1, Ground Floor.

NOTES TO EDITORS:

1. *Fiscal Assessment Report, November 2013* is under embargo until 00.01 a.m Friday 22nd November. The report will be available to download from www.fiscalcouncil.ie
2. *Fiscal Assessment Reports* are submitted to the Minister for Finance and laid before the Oireachtas.
3. The Council is chaired by Professor John McHale, NUI, Galway. The other council members are Mr Sebastian Barnes, Professor Alan Barrett, Dr Donal Donovan and Dr Róisín O'Sullivan.

The following is the Summary Assessment from the *Fiscal Assessment Report, November 2013*.

Further progress is being made in repairing the public finances, but changes to planned budgetary adjustments have removed the margin of safety.

- Good progress continues to be made in bringing sustainability to the public finances and restoring the borrowing capacity of the State. The General Government debt-to-GDP ratio is projected to peak this year at 124.1 per cent before declining by approximately 10 percentage points over the period to 2016. Overall, the Government's planned fiscal stance is assessed to be conducive to "prudent economic and budgetary management".
- However, the decision to reduce the planned fiscal adjustment in *Budget 2014* has eliminated the previously existing margin of safety relative to the key 3 per cent Stability and Growth Pact deficit ceiling for 2015. An analysis based on historic growth forecast errors suggests that the probability of breaching the 3 per cent ceiling has risen from an estimated 1-in-3 to an estimated 1-in-2, assuming no changes in planned adjustments for Budget 2015.
- There should be no reduction in the Government's previously announced adjustments of €2 billion for 2015.

The Council has endorsed the macroeconomic projections underlying Budget 2014.

- Under new EU requirements, the Council has been tasked with independently scrutinising and endorsing the macroeconomic projections underpinning Budgets and Stability Programme Updates. This is a significant change in Ireland's budgetary architecture and should help to improve the accuracy and transparency of official macroeconomic forecasts. The Council has developed its own forecasting methods and analytical capacity to support this function. The approach to the endorsement exercise is described in detail in this report.
- The Council's endorsement is based on whether the forecasts are within an endorseable range of appropriate forecasts, taking into account the methodology and the plausibility of the judgements involved. This range reflects, in part, the uncertainty surrounding any growth forecast.
- As part of the endorsement exercise, the Council expressed a significant reservation about one element of the macroeconomic forecasts prepared for *Budget 2014*. This reservation related to the implied quarterly profile for consumption spending. However, following clarifications by the Department of Finance on the assumptions relating to data revisions, the Council assessed that the forecasts were within its endorseable range.

But risks are tilted to the downside.

- The Department of Finance is projecting real GDP growth of 0.2 per cent in 2013, rising to 2 per cent in 2014. Growth this year is being depressed by a number of factors. These include a background of ongoing balance sheet repair, budgetary consolidation and weak demand in Ireland's main trading partners. The pharmaceuticals "patent cliff" is also reducing the growth of net exports. Uncertainties relating to these elements mean that risks to the forecasts are tilted to the downside for 2014.

Budget projections are assessed to be appropriate.

- The budgetary projections in *Budget 2014* are assessed to be appropriate, but are contingent on the delivery of significant expenditure savings and achieving the projected acceleration in economic growth. Additional risks stem from contingent liabilities associated mainly with the banking sector.
- There was some public confusion on the size and composition of the budgetary adjustment contained in *Budget 2014*. Notwithstanding welcome recent improvements in fiscal reporting, future Budget statements should identify clearly the impacts of consolidation measures.

And budgetary projections are consistent with compliance with all national and European fiscal rules.

- *Budget 2014* projections imply compliance with the national Budgetary Rule in 2013 and in each forecast year out to 2016. This is because the Adjustment Path Condition for the structural balance to converge towards Ireland's Medium-Term Budgetary Objective (MTO) is met.

The Council would have supported an application for a precautionary credit line.

- Given a fragile international financial environment, the Council would have supported an application for a precautionary credit line. Provided it had come with reasonable terms and conditions, such a facility would have provided valuable additional protection against any renewed funding pressures as Ireland exits the EU/IMF assistance programme.